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SMART STRATEGIES
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Jagruti Finance Ltd/ SmartPay Bank

A CASE STUDY

Jagruti Finance Ltd (JFL), a subsidiary of diversified Indian company, INR 86000 crore Pune-based Jagruti Group, is one of the largest Non-Banking Financial Company (NBFC) in India, which has been operating since 1999. Started as a consumer finance company to fund the purchases made by the consumers in the large format stores operated by its parent company, JFL soon got into education loans, after its parent company diversified into education area. Since then, it has also got into vehicle finance and travel finance, in tie-up with three of India's largest travel agencies. In fact, it is the largest travel finance NBFC in India. It has also got into commercial finance in the last six years. It got into limelight when it became one of the first Indian finance companies to get into a trade-finance blockchain pilot with automobile major, Mudra Suave Ltd.

JFL's 2018-19 turnover was INR 7200 crore, with a net profit of INR 972 crore. The revenue growth was 16%, while the net profit grew by 22%.

In 2013, JFL took a license to offer e-wallet services, after acquiring a technology company, which was working on the payment space. Branded SmartPay, JFL's payment services started well by offering one of the best experiences, but it fell behind in the post demonetization period as cashbacks and wider reach propelled other brands to leadership positions. It is still among the top five payment players, largely driven by bill payment and by operating the loyalty wallet of its parent company's four branded retail chains.

JFL forayed into Payment Bank business by obtaining an approval from RBI in 2015. Called SmartPay Bank (SB), the new entity started

operations in February 2017. It is also headquartered in Pune.

JFL hired Shashi Bhushan Pandey, a banking industry veteran to head SmartPay Bank as CEO. Interestingly, after CEO and CFO Nikhil Jain, the third executive hired by the bank was its Chief Technology Officer. CTO Vinay Bhushan has worked in both the industry side—in the payment domain—and in user companies—as CIO in two leading banks, one payment startup and an NBFC.

Operations & Ratios

SmartPay Bank was one of the first Payment Banks to become operational. It has now operated for two full financial years.

SmartPay Bank operates in twelve locations in Maharashtra and Gujarat with 23 branches and is supported by 36 ATMs. It also has a tie-up with Marathwada-Konkan National Bank (MKNB), an Old Private Sector Bank, whose ATMs can be used by SmartPay Bank's users. It also distributes some products of MKNB. Since a Payment Bank cannot accept deposits for more than INR 1,00,000, SmartPay Bank has tied up with MKNB to provide its customers the facilities to do that with MKNB.

Like all other Payment Banks, SmartPay Bank is operating at a



loss. In the year 2018-19, it earned an interest income of INR 7 crores and other income of INR 33 crores. Net Interest Income was around INR 5 crores. While Operating Loss was INR 14 crores, it made a Net Loss of INR 12 crores.

It has mustered a total deposit of INR 11 crores so far.

Almost all the ratios, though still worrying, have improved. In FY 19, Return on Asset (RoA) of SmartPay Bank improved to -6.6% from -9.2%, while Return on Equity changed to -18.2% from -21.2%. Net Interest Margin as well

as Cost-Income Ratio have also shown improvements.

From the initial set of payment banks which were given approval by RBI, four backed out even before beginning. Out of the rest, two were struggling to start. From the rest, one has already declared this year that it would cease operations, calling the business unviable.

SmartPay Bank is one of the few payment banks who are still holding on. Good news is that their operational metrics are improving; bad news is that, they still have a long way to go for profitability. But SmartPay Bank is willing to play for the long-term.

IRDA and SEBI respectively, with distribution and sales commission capped. Secondly, they require highly trained manpower who understands those products. Hiring better quality manpower and training them without adequate volume of business is a risky proposition. SmartPay Bank distributes insurance products of two life insurance and one general insurance companies. But with small deposit and limited mandate, customers see payment banks as just another set of payment provider and hence always look out for better pricing on transactions. As a result, there is hardly any deeper engagement with customers. Typically, cross-selling works best when a service provider has very deep relationship with the customer. With the absence of that, payment banks still struggle to cross-sell.

While SmartPay Bank has seen some good traction in specific categories of General insurance—especially travel and vehicle—owing to its parent company’s strengths, life insurance distribution has been a non-starter.

It has done much better in distribution of credit products though. It has managed to sell loans from its own parent JFL as well as from MKNB. In fact, it is the No 1 among payment banks in this category—by a big margin.

To provide safety nets to customers, RBI has stipulated that payments banks should invest 75% of their Current Account Savings Account (CASA) balances in Statutory Liquidity Ratio (SLR) eligible government

SmartPay Bank: Key Financials	
Metrics	Amount (INR Cr.)
Total Capital Reserve	46
Deposits	11
Cash & Balance with RBI	9
Balances with Banks & Money Markets	30
Investments	65
Fixed Assets	7
Other Assets	18

SmartPay Bank: Key Ratios	
Ratio	Value (%) (2019)
Return on Assets	-6.6
Return on Equity	-18.2
Investments to Total Assets	50.1
Net Interest Margin	6.5
Efficiency (Cost-Income Ratio)	122.2
Operating Profit to Working Funds	-10.7
Profit Margin	-36.4

Challenges & Opportunities

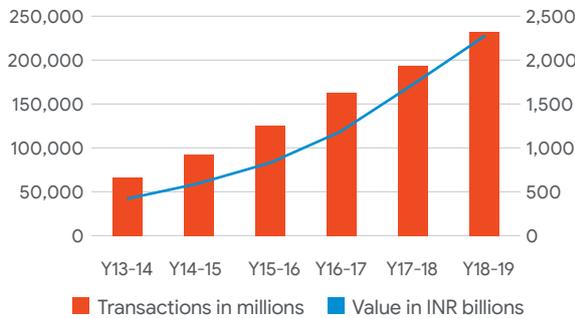
The choice before payment banks to earn is limited. Digital payments, while growing fast, is only a limited option. Both Scheduled Commercial Banks (SCB) on one side and payment providers—from small FinTechs to Google and Amazon—on the other, everyone is targeting a slice of the pie. Large payments are still happening over the NEFT and RTGS route where there is a significant advantage enjoyed by SCBs. A payment bank can accept deposits worth only one lakh rupees; so, payment over NEFT cannot be too high.

Cross-selling of other financial products like insurance, bonds and mutual funds has been touted as a great opportunity. But selling of insurance and mutual funds are highly regulated by

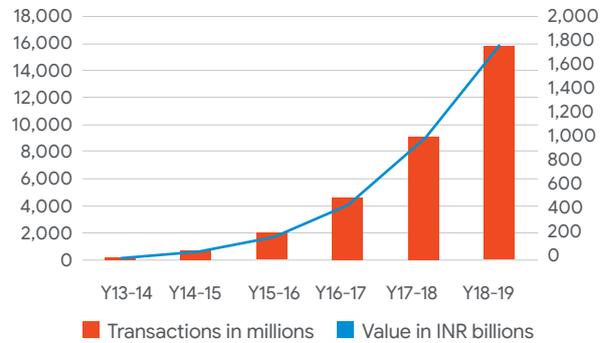
Payment Trends in India*

How various payment modes have grown in India in the last five years

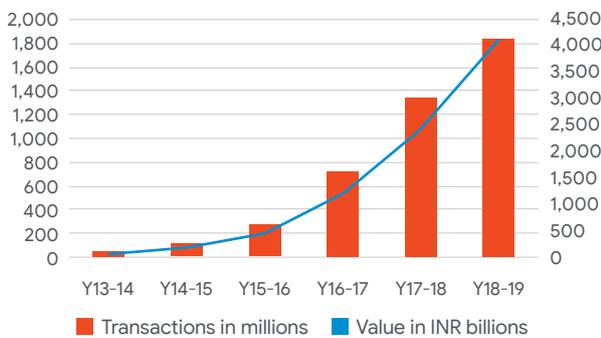
Growth of EFT/NEFT



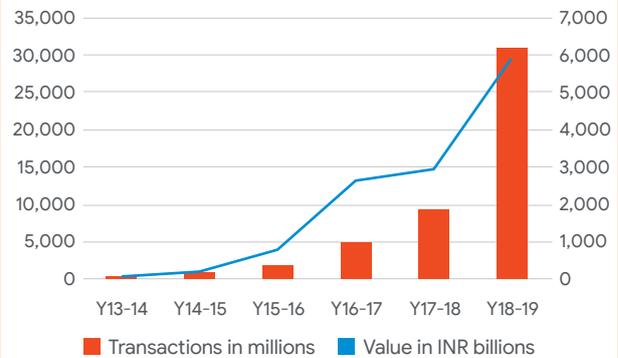
Growth of IMPS



m-wallet Usage



Mobile Banking



*Data source: RBI

bonds or T-Bills. It severely restricts their ability to optimize utilization of the money.

But the most profitable area for commercial banks are working capital loans, business loans and credit cards, which payment banks are barred from providing because they are not permitted to lend at all.

Also, with Aadhaar becoming voluntary, KYC cost has risen up substantially. For the segment of users that payment banks target, it is even costlier. That is pinching the payment banks.

In short, payment banks are struggling to even survive. Maybe, RBI will eventually allow them to

broaden their portfolio. But they have to first survive now to see that day.

Shashi B Pandey, the CEO of SmartPay Bank is hopeful, though. He points to the potential opportunities.

India has huge unbanked population. Many Jan Dhan account holders have not done any transaction other than cashing out their benefits. A large number of them do not even use the accounts. It is these bottom-of-pyramid segments that he sees huge opportunity in.

Of course, digital payments are growing rapidly. In the last five

years, IMPS payment has grown 150 times by value while m-wallet payment has grown 55 times! There is a huge opportunity to try out innovative payment products.

SmartPay Market Strategy

“It is only by reducing the cost of transactions (that) we can reach all,” the famous comment of Raghuram Rajan, the erstwhile governor of RBI, is framed in SmartPay Bank CEO Pandey’s office.

“The cost structure in the banking system despite use of all the

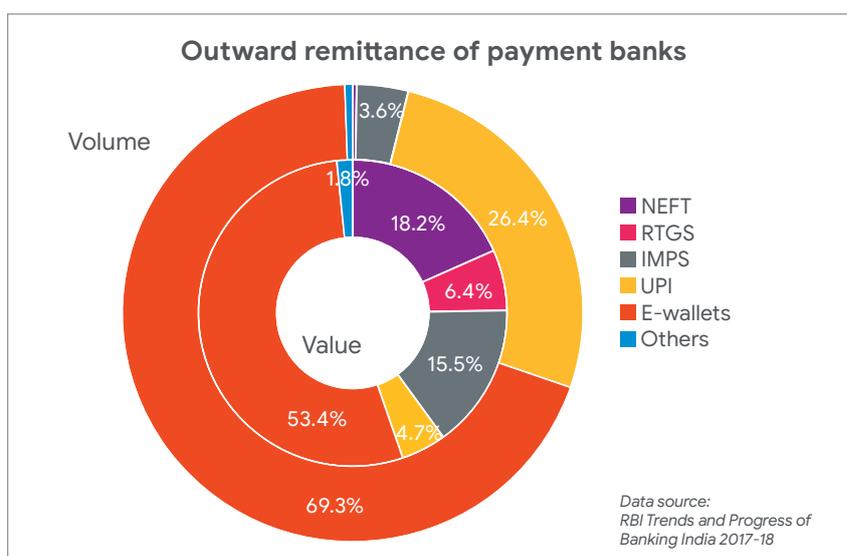
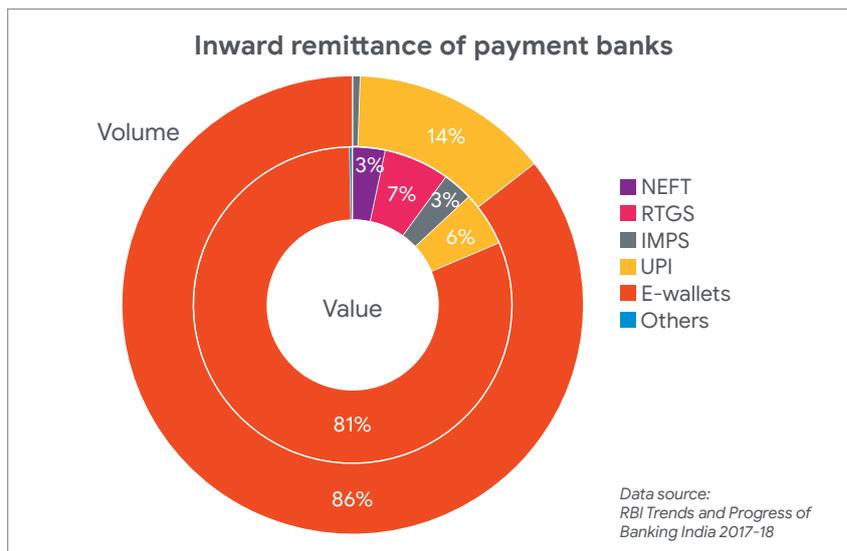
information technology is still significantly high. We can see the effect of the IT revolution everywhere in the banking system, except on the expenses side. Why aren't the expenses coming down?" Rajan used to ask many a times.

Pandey says that precisely should be the Holy Grail of every Payment Bank—reducing the cost of transaction and making banking affordable.

He has a four-point strategy for driving SmartPay Bank's growth. Acronymed CLUE, they spell out what SmartPay Bank should do in the initial phases of growth.

They are:

- **Cross-selling:** Identifying the right array of services to cross-sell. SmartPay's success in selling general insurance products has been a result of this thrust.
- **Lower Cost of Transaction:** The most important element of his strategy is to use various means—most importantly technology—to lower the cost of transaction.
- **Urban low-income user as a target segment:** While most commercial banks are after the high- and middle-income customers and policy initiatives are mostly targeted at benefitting the rural customers, Pandey's commissioned research has found that there is a huge opportunity in low-income urban consumers. They use most of the services, especially payment services, and yet the transaction value is low. They are ideal customers for payment banks, he thinks.



- **Experience:** 'We are a bank, not an apology,' says Pandey. He says despite RBI restricting the portfolio of services and despite their's being a low-cost operation, they can still provide an experience, especially to the low-income urban users who do not get that anywhere.

Pandey believes once the bank reaches a critical mass, many of the other handicaps would automatically be removed. That is a chicken-and-egg story. The JFL board backs Pandey solidly and wants to stay in the game long-term.

Tech is the Answer

"The payments bank is expected to leverage technology to offer low cost banking solutions," said RBI's guidelines on payment banks. Despite a lot of constraints, most payment banks are trying to leverage technology to compete.

The hiring of a CTO by SmartPay Bank even when its business model was not finalized is a testimony to this reliance on technology.



Next Target

CEO Pandey has mandated CTO Bhushan to divide the tech strategy—the priority, the resources, and the investments—into three buckets. They are:

1. Tech required to run the basic business and to meet RBI's compliance requirement
2. Tech needed to drive the four-point strategy
3. Tech that can help bring in small differentiations, competitive advantages, even if tactical

While the payment banks are allowed to offer only a limited range of services, many of the compliance requirements for scheduled commercial banks and small finance banks are also applicable for payment banks. For example, RBI says that while offering internet banking services, “the payments bank will be required to comply with RBI instructions on internet banking; and information security, electronic banking, technology risk management and cyber frauds,” applicable to other banks as well.

“The operations of the (payment) bank should be fully networked and technology driven from the beginning, conforming to generally accepted standards and norms; while new approaches (such as for data storage, security and real-time data updation) are encouraged, a detailed technology plan for the same should be furnished to RBI,” says the guidelines explicitly.

Further, rules such as data residency (all data should stay on Indian soil) applicable to commercial banks are also

applicable to payment banks.

SmartPay has invested in a version of Finacle core banking solution specially designed for payment banks. It runs from a data center co-located with its partner scheduled commercial bank, MKNB's data center in Mumbai. It has a small DR center in its premises in Pune.

The payment solution designed in-house by parent, JFL, is used by SmartPay Bank. The integration of core banking and the digital wallet solution are still not complete.

It has also invested in a homegrown CRM system that runs in premise for part of its operations and on a SaaS model for other parts. It is critical to its distribution (cross selling of other financial products) business.

SmartPay Bank provides Internet banking facilities and also supports most of its services through a single mobile app. Some of the basic transactions like balance enquiry, last five transactions and ATM locations can be done on SMS too.

In its tech adoption cycle, the first bucket is by and large stable, though the integration of payment and core banking is still to be completed due to which a single view of customer is a challenge.

For cross-selling, SmartPay wants to get an analytics-leveraged platform and AI-based customer relationship management that should be simple, manageable and low-cost, if not feature rich.

The most important component in the strategy is continuously lowering the cost of operations. Bhushan is working on shifting to cloud but wants to be doubly sure about security and compliance. Of course, data has to stay in India.

The third strategy—differentiation for urban low-income customers—is the biggest challenge for Bhushan and his team. Quite a few of the targeted users use smartphone, but some do not. While specific apps are an obvious idea, the facilities, should be made available to non-smartphone users in some way. That is a big challenge.

As far as experience is concerned, the reliance is heavy on technology. Apps, especially that incorporate video conferencing, have been actively discussed, even though they know that reach of smartphone in targeted user segments is limited. But looking at the falling data rates and growing smartphone penetration, SmartPay Bank is betting on apps and is putting a lot of energy into differentiated apps. It would like to keep the cost of development really low.

Beyond these, two specific areas are priorities for SmartPay Bank. The first is a cost-effective and flexible data management platform that can scale easily, even though the bank can expect limited returns from such a system at present. Two, SmartPay is

investing significantly on security solutions and even talks about it explicitly.

Your Task

Your brief is to do a tech assessment and create a tech plan that should be in sync with the three broad buckets of technology plans of SmartPay Bank. You should explicitly translate the strategies into tech plans.

Please ensure that the technology plan should have the following:

- Insights from current need assessment
- A clear business outcome associated with each tech initiative or investment
- It should be detailed enough

to illustrate what are the components/solutions and what technology(ies) will each of the components

- It should be mapped to the three buckets – stated strategy; compliance and basic operations; and finally, tactical stand-alone initiatives
- There should be a roadmap—with timelines and priorities. Please justify your prioritization
- It should only use the technologies presented to you today
- Give budgets, resources, and challenges
- Make suitable assumptions as long as they do not contradict any of the given facts



Current IT Environment @SmartPay Bank

Software: Finacle Core Banking System (CBS) for payment banks; CRM and Marketing Solution, a local Business Intelligence System, Document Management System, Fraud Detection and Surveillance Solutions, an Asset Management Solution, HR System.

Infrastructure: A data center co-located with its another commercial bank, MKNB's data center in Mumbai. A small DR center in Pune.

